

To the Mayor and Members of the City Council**July 28, 2015****SUBJECT: NON-INSURANCE INTERNAL SERVICE FUNDS RESERVE POLICIES**

Over the course of the last several months, Staff has undertaken an intensive project to do a thorough review and update of the Reserve Policies for all City funds.

Currently, the following revisions to the FMPS reserve policies have been approved by City Council: M&C G-18466 revised the Reserve Policies for the City's Governmental Funds (General Fund, Special Revenue Funds, Capital Project Funds, and Debt Service Fund). In addition, M&C G-18940 approved the Reserve Policy for the City's Insurance Type Internal Service Funds.

This informal report is intended to provide background and information on the next policy revision proposed by the Department of Finance regarding all Non-Insurance Type Internal Service Funds, including the: Equipment (Fleet) Services Fund, Information Technology Systems Fund (ITS), and the Capital Projects Service Fund.

What is an Internal Service Fund?

Internal Service Funds are used to report any activity that provides goods and/or services to other funds, departments, or agencies for the benefit of the primary government and its component units. These funds "charge" other funds/departments for the services they provide to generate revenue to support their operations.

Recommended Reserve Policy

The Department of Finance proposes the following Reserve Policy for all Non-Insurance type Internal Service Funds:

- A minimum level of working capital that equates to three (3%) percent of on-going operating expenses.
- In addition, no Internal Service Fund shall have a negative Unrestricted Net Position.

In the existing FMPS there is currently no minimum reserve requirement for Internal Service Funds.

While the recommended reserve level is lower than those adopted for other fund types, the Non-Insurance type Internal Service Funds do not generally have large capital expenditures or carry debt. Further, they do not have the claims-and-liability exposure of the Insurance Type Internal Service Funds. Because of the less volatile risk profile of these funds, a minimal reserve for the Non-Insurance Type Internal Service Funds is recommended.

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Impact of recommended reserve policy (as of 9/30/14):

The impact of the proposed policy on each of the specific funds is detailed below.

Equipment (Fleet) Services Fund:

- Unrestricted Net Position – (\$2,920,000)
- Working Capital – (\$1,033,000)
- 3% of Operating Expenses - \$804,840
- Over (Under) Based on Unrestricted Net Position - (\$2,920,000)
- Over (Under) Based on Working Capital – (\$1,837,840)
- Available for Use – N/A

In order to address the shortage of reserves based on the recommended policy, the Equipment (Fleet) Services Fund has implemented a three year program to contribute resources to net position. For fiscal year 2015, the fund is anticipated to accumulate \$653,000 in excess revenues, and slightly higher amounts are anticipated in FY2016 and FY2017. These contributions will be reviewed on an annual basis with the intent to move the fund to be in compliance with the revised policy minimum reserve.

Information Technology Systems Fund (ITS):

- Unrestricted Net Position - \$4,442,000
- Working Capital - \$4,811,000
- 3% of Operating Expenses - \$790,050
- Over (Under) Based on Unrestricted Net Position - \$3,651,950
- Over (Under) Based on Working Capital - \$4,020,950
- Available for Use - \$4,020,950

The ITS Fund is in a unique position – as of the end of fiscal year 2014, the fund has resources in excess of the proposed policy. These monies have been appropriated during fiscal year 2015 to the IT capital project fund to be used in replacing the City's telephone system as well as improving the City's network infrastructure.

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- Unrestricted Net Position – (\$3,258,000)
- Working Capital – (\$940,000)
- 3% of Operating Expenses – \$356,820
- Over (Under) Based on Unrestricted Net Position – (\$3,258,000)
- Over (Under) Based on Working Capital – (\$1,296,820)
- Available for Use – N/A

In order to address the shortage of reserves based on the recommended policy revision, staff is working on several different options, which include utilizing funds from other sources and a multi-year plan to contribute to net position. Both options are being evaluated by management in order to ensure a comprehensive solution.

If you have any questions, please call Aaron Bovos, Chief Financial Officer, at 817-392-8517.

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City Manager